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No. 86-784

In the Supreme Court of the United States

OCTOBER TERM, 1986

SILAS V. CROSS, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA AND THE COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENTS IN OPPOSITION

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TABLE OF AUTHORITIES

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Petitioners contend that the federal income tax does not apply to members of Indian tribes. They also contend, in the alternative, that income earned from the operation of a smokeshop located on the Puyallup Indian Reservation is exempted by treaty or by statute from federal taxation. The court of appeals correctly rejected these contentions. Its decision does not conflict with any decision of this Court or of another court of appeals, and there is no reason for further review.

1. Petitioner Silas V. Cross, a noncompetent,[1] enrolled member of the Puyallap Indian Nation, operated a smokeshop in the Puyallup Indian Reservation on land first allotted to his grandfather in 1886. In 1976, he had a net profit of $41,687 from the sale of cigarettes and other tobacco products and merchandise in the smokeshop, but he failed to report the income received from the smoke-

[1] The term "noncompetent" refers to the status of an Indian to whom land, held in trust by the United States for his benefit, has been allotted, but who cannot alienate or encumber that land without the consent of the United States.

shop on his federal income tax return for 1976. His son, petitioner Silas A. Cross, who is also a member of the Puyallup tribe, received $1,899 in wages for working in the smokeshop during 1976. He did not report those wages on his return for 1976. The Commissioner determined that the profits earned by Silas V. Cross and the wages received by Silas A. Cross were includable in their respective incomes and, accordingly, asserted deficiencies in their taxes. Pet. App. AA52-AA53.[2]

Petitioners sought redetermination of the deficiencies in the Tax Court, which upheld the Commissioner's determination in a reviewed decision (Pet. App. AA48-AA81). The court rejected petitioners' claim that Indians are not liable for the payment of federal income tax (*id.* at AA53-AA54). With respect to the smokeshop income, the court held that the Medicine Creek Treaty of Dec. 26, 1854, United States—Nisqually Tribe, 10 Stat. 1132 *et seq.*, did not create any exemption from federal income taxation (Pet. App. AA55-AA57). And the court held that the tax exemption for income "directly derived" from allotted reservation land (see *Squire* v. *Capoeman,* 351 U.S. 1 (1956)) is not applicable to wages and profits derived from a retail business that involves no exploitation of the land (Pet. App. AA57-AA61). Finally, the court rejected petitioners' alternative argument that the smokeshop income should be exempt under *Capoeman* at least to the extent that it equated to an imputed fair rental value for the land (*id.* at AA61-AA66). Five judges dissented on this latter point (*id.* at AA68-AA81).

Petitioners' appeal was consolidated in the Ninth Circuit with three other appeals taken by other members of the Puyallup Indian Nation, all of which involved taxation of smokeshop income. The court of appeals unanimously affirmed in all respects (Pet. App. AA1-AA27).

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[2] Petitioners Millie Cross and Francine Cross are the wives of Silas V. Cross and Silas A. Cross, respectively. They are parties to this case solely by virtue of having filed joint 1976 tax returns with their respective spouses.

2. Petitioners' principal contention (Pet. 6-14) is that Indians, or at least noncompetent restricted Indian allottees, are not subject to the federal tax laws. This contention is wholly without merit. By its terms, the federal income tax applies to "every individual" and to "all income from whatever source derived." Internal Revenue Code §§ 1, 61 (26 U.S.C.). It is well settled that Indians, like other citizens, are subject to payment of federal income taxes unless an exemption from taxation can be found in the express language of a treaty or an Act of Congress. See, *e.g.*, *Squire* v. *Capoeman,* 351 U.S. 1, 6 (1956); *Superintendent* v. *Commissioner,* 295 U.S. 418, 419-420 (1935); *Choteau* v. *Burnet,* 283 U.S. 691, 693 (1931). As stated in *Capoeman,* 351 U.S. at 6, "Indians are citizens and * * * in ordinary affairs of life, not governed by treaties or remedial legislation, they are subject to the payment of income taxes as are other citizens." Petitioners' contention (Pet. 6-9) that Indians are not citizens of the United States is plainly wrong. Citizens of the United States are defined by statute to include "a person born in the United States to a member of an Indian, Eskimo, Aleutian, or other aboriginal tribe" (8 U.S.C. 1401(b)).[3]

3. Petitioners contend (Pet. 11-13) that Article 6 of the Medicine Creek Treaty of 1854 exempts their smokeshop

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[3] Petitioners' contention (Pet. 9-10) that the decision below conflicts with *United States* v. *Daney,* 370 F.2d 791 (10th Cir. 1966), is fanciful. The Tenth Circuit did not hold in *Daney* that Indians are not ordinarily subject to the federal tax laws; it simply recognized that certain income of a noncompetent Indian living on alloted land may be exempted from tax by treaty or statute. In *Daney,* the court held that an express statutory exemption for land held by members of the Five Civilized Tribes of Oklahoma applied to a bonus received by a member upon execution of a lease of oil and gas rights. The court of appeals in this case similarly recognized that treaties or statutes may grant Indians a tax exemption not available to other citizens. The court concluded, however, that there was no such exemption applicable to the income at issue here.

income from tax. This contention was correctly rejected by the court of appeals (Pet. App. AA8-AA10). Article 6 incorporates an agreement providing that property allotted under the treaty "shall be exempt from levy, sale or forfeiture" (Pet. App. A29; *id.* at AA8-AA9). This language does not purport to establish a tax exemption, and it is patently insufficient to do so. An intent to exclude Indians from taxation must be "definitely expressed." *Choteau* v. *Burnet,* 283 U.S. at 696; see also *Mescalero Apache Tribe* v. *Jones,* 411 U.S. 145, 156 (1973). The treaty language cited by petitioners does no more than prohibit forced transfers of Indian property until the property comes under the jurisdiction of a state constitution. This restriction on alienation of Indian property (established before there was a federal income tax) cannot reasonably be construed as creating a tax exemption for income derived from retail businesses operated on Indian land. See *Superintendent* v. *Commissioner,* 295 U.S. at 421 ("Nontaxability and restriction on alienation are distinct things.").

4. Petitioners contend (Pet. 13-15) that the court of appeals erred in construing the tax exemption established in *Squire* v. *Capoeman* as applying only to income "directly derived" from allotted trust land (see Pet. App. AA14-AA21).[4] This contention is without merit. In *Capoeman,* the Court held that the government's obligation under the General Allotment Act of 1887, 25 U.S.C. 331 *et seq.*, to transfer allotted trust properties at the end of the trust period "free of all charge or incumbrance" required that income "derived directly" from such properties be exempted from taxation. See 351 U.S. at 9. Applying that rule, the Court disallowed federal taxation of income from

[4] Petitioners do not appear to challenge the court of appeals' application of its construction to the particular facts involved here, and they clearly do not renew in this Court their contention below that an amount equal to the fair rental value of the land should be exempted from taxation.

the sale of standing timber on allotted lands, but allowed taxation of "reinvestment income" (*ibid.*). In the wake of *Capoeman,* the lower courts have consistently drawn a distinction between income derived directly from the allotted trust land, which is tax exempt, and income only indirectly related to the land, which is not tax exempt. See, *e.g., Critzer* v. *United States,* 597 F.2d 708, 712-714 (Ct. Cl.), cert. denied, 444 U.S. 920 (1979) (income from motel, restaurant, and gift shop not exempt); *Hayes Big Eagle* v. *United States,* 300 F.2d 765, 770 (Ct. Cl. 1962) (royalty income from mineral extraction exempt); *Hale* v. *United States,* 579 F. Supp. 646 (E.D. Wash. 1984) (rental of improved property not exempt); *Hoptowit* v. *Commissioner,* 78 T.C. 137 (1982), aff'd on another issue, 709 F.2d 564 (9th Cir. 1983) (smokeshop income not exempt). This distinction is soundly based in the express language of *Capoeman* and is fully consistent with the scope of the General Allotment Act. Hence, the income earned by petitioners in the form of wages and profits from the operation of a retail smokeshop on their allotted land, which clearly was not derived directly from that land, is subject to federal income taxation.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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